The Heritage Foundation Backgrounder

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BRINGING ANTITRUST LAWS INTO THE TWENTIETH CENTURY

INTRODUCTION

Growing trade deficits are focusing attention on problems faced by U.S. producers in world markets. Having once enjoyed what appeared to be an unassailable position as the world's commercial leaders, U.S. companies hold decreasing shares of the market, which is causing serious trouble for businessmen, labor leaders, and politicians.

The answers most commonly proposed are protectionist. Foreign competitors are said to enjoy an unfair advantage because of the availability of cheap labor or subsidies provided by their governments. Thus, domestic content legislation, tariffs, import quotas, and other trade barriers are urged on Congress and the Administration. Yet such solutions at best would provide very short-term relief for the industries targeted. In the long run, such policies would cost many more jobs than they saved. The true challenge before Congress is not to erect barriers to foreign goods but to identify the structural problems and treat the causes of U.S. competitive difficulties.

One major structural problem is America's antiquated web of antitrust laws. The enforcement of these laws has inhibited the adjustment of American industry to changing world market conditions in several important ways.

Recently, efforts by the LTV Corporation and Republic Steel to merge, forming a single firm better able to meet foreign competition, were hindered by Justice Department objections. If there is a textbook example of a declining U.S. industry that should be allowed to consolidate its resources in order to modernize and survive, it is the U.S. steel industry.[1] Fortunately,

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1 Naturally, this streamlined steel industry should also be forced to forgo current protections against foreign competitors. An open market is the consumers' best guard against abuses of market power.

Note: Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

the Justice Department and the affected firms were able to reach an agreement that will allow the merger to go forward. But the costs involved--in time, legal fees, forgone opportunities--seem an unnecessary additional burden for an already troubled industry. And the resultant delays are bound to produce a chilling effect on other possible mergers within the industry.

Besides this excessive concern about domestic market shares in an era of stiff international competition, the antitrust laws have further hindered U.S. competitive success by sending a clear signal that it does not pay to be too successful. Since the Sherman Act was first passed, industry leaders have frequently found themselves subject to expensive, time-consuming antitrust battles brought on by their market success. This has been true where leadership was gained through more efficient production and lower prices for consumers as well as cases of innovative accomplishment. Indeed, in a 1980 Federal Trade Commission case, DuPont was charged with "attempting to monopolize" because its research staff had discovered and patented a less expensive means of recovering a particular chemical, and DuPont had the audacity to pass the savings along to its customers. "Unfair competition," charged the FTC legal staff. By forcing its competitors to match its price cuts, DuPont was preventing them from generating funds with which to pursue their own research in the area.[2]

Surprisingly, however, the federal government is not the greatest offender in this area. Private antitrust cases account for the lion's share of those brought, and these private litigants are often more interested in obstructing and delaying actions by their competitors than they are in righting any real wrongs. Thus, the antitrust laws can be shown to discourage both product and process innovation and inhibit firms attempting to achieve economies of scale. The incentive structure thus created punishes Americans as consumers first, and as a labor force second. By inhibiting increased efficiency, delaying expanded research and development, and retarding continued modernization, U.S. antitrust laws have left American industry ill-prepared to compete in an international market.

Current antitrust policies, therefore, should be reconsidered to enable firms to undertake orderly reorganization and expansion. By failing to recognize the growing importance of today's world market, the antitrust laws make it unnecessarily difficult for U.S. firms to compete with foreign firms. Market realities and the sophistication of economic analysis have changed substantially since 1890 when the Sherman Act was passed. These changes now must be reflected by revising the statutes.

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[2] Betty Bock, The Innovator as an Antitrust Target, Information Bulletin No. 174, The Conference Board, 1980.

The Sherman, Clayton, and Federal Trade Commission Acts, the three pillars of antitrust law, should all be modified to protect the competitive process and consumers rather than individual competitors. Furthermore, existing incentives for private antitrust nuisance cases should be removed. Finally, conflicts between laws encouraging creativity and innovation and the antitrust laws should be resolved with a tilt toward innovation.

THE THEORY OF ANTITRUST POLICY

Federal antitrust policy began in 1890 with the Sherman Act, which sought to prohibit monopolies and activities that constrained trade. The Clayton and Federal Trade Commission Acts were added in 1914. Clayton outlaws specific trade practices not covered by Sherman and attempts to restrain the growth of monopoly in its "incipiency" (i.e., before Sherman violations can develop). Early proponents of such restrictions also felt an agency should be created, with competence in business affairs, to perform investigatory and adjudicative functions. The result was the Federal Trade Commission Act. It established the FTC and outlawed "unfair and deceptive methods of competition," leaving the Commission, and ultimately the courts, to determine exactly what practices fit this description.

Inadequacies of the "Perfect Competition" Approach to Antitrust

The FTC, the Justice Department, and the antitrust courts long have used the economic model of "perfect competition" as an ideal when interpreting the antitrust laws. A perfectly competitive market must meet several criteria. It must contain a large number of buyers and sellers, all with perfect information about market conditions--especially prices. The products sold by the various firms must be identical, so customers will have no firm preferences or brand loyalties. And each firm must be small relative to the market as a whole so that the entry or exit of any one firm will have no effect on market price. Under these conditions, no firm can charge more than the prevailing market price because it will lose all its customers. Likewise, there is no reason to charge less than the market price, because each firm can sell all it wants at the prevailing rate.

Theoretically, perfectly competitive markets are appealing. Firms earn just enough profit to stay in business, but no more. They use their resources efficiently or incur losses that, if allowed to continue, will drive them from business. Thus, consumers are well served, receiving goods competitively produced at the lowest price possible, given the cost and availability of resources.

While useful in the academic world, however, this model has serious shortcomings when applied to actual markets as a benchmark for antitrust policy. The perfect competition model may portray

a market's state at a given point in time, but like a photograph, it does not reveal how the market got where it is or indicate where it is going. Examples: What happens if one firm discovers a better production process or makes a significant improvement in the product? How are consumers able to obtain complete price information, and what happens if they have incomplete data? How does the market change if one firm begins offering additional service with its product or if there is a sudden shift in the demand for the product or in the supply of inputs?

How a Bad Model Leads to Bad Decisions

Given the static nature of the perfect competition model and its stringent requirements, it is not surprising that antitrust courts have found almost no examples of the ideal industry. Most U.S. firms enjoy some "market power," that is, they have some control over the price and quality of the products they sell. In fact, any sort of product differentiation can give a firm this "power." The firm's location may provide such an advantage. Consumers without instant access to information concerning prices charged by all sellers also provide firms with market power. And brand or firm loyalty increases a businessman's control over the price of his product.

The acceptance by the antitrust courts of perfect competition as a goal and the subsequent observation of some market power in almost all industries have led antitrust enforcers to challenge a wide variety of seemingly insignificant actions.

Horizontal Concentration: In 1966, for example, the Supreme Court struck down a merger between two grocery chains in Los Angeles, which would have produced a firm with 1.4 percent of the stores and 7.5 percent of the sales in that market.[3] The decision was based on the observation that the number of single-store owners had declined substantially as grocery chains became increasingly important.[4] To derail this trend toward concentration "in its incipiency," the Von Grocery merger was denied--even though it could have created efficiencies that allowed the merged firm to compete more effectively against other grocery chains.

Vertical Concentration: Almost as dangerous as horizontal mergers, in the view of some courts, are vertical arrangements that provide an advantage over competitors. For example, mergers between manufacturers and retailers leading to more efficient product distribution have been suspect because the industry might become more concentrated--especially if other firms are driven out of business because of the merger or find similar arrangements necessary if they are to compete effectively. In Brown Shoe, for

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3 Robert H. Bork, The Antitrust Paradox: A Policy at War with Itself (New York: Basic Books, 1978), p. 217.

4 Ibid., p. 219.

instance, the Supreme Court ruled in 1962 that this suspicion applied even to firms with seemingly insignificant shares of the market. The Brown Shoe Co., primarily a shoe manufacturer, was prohibited from acquiring G. R. Kinney Co., primarily a shoe retailer, even though Brown controlled only 4 percent of the nation's shoe output, and Kinney had 1.2 percent of total national retail shoe sales. In writing the decision, Chief Justice Earl Warren made it clear that small producers were to be protected from the presumed possibility of market manipulation--even at the expense of consumers who would have gained from efficiencies resulting from mergers.[5]

Oligopolies: Especially troubling to antitrust enforcers have been "oligopolies," that is, industries containing only a few large firms. When perfect competition is the benchmark, highly concentrated industries present serious potential problems. Not only are the individual firms suspected of exercising substantial market power, but they also present the added danger of cartels. Indeed, in those industries where one or two firms are clearly dominant, a formal agreement is assumed to be unnecessary for restraint of trade to occur.

This presumption that concentrated industries are almost inherently evil has led to a number of antitrust cases against industry leaders--even when those firms clearly attained their positions through greater efficiency or ambitious innovation. Examples include the Standard Oil of New Jersey case (1911), the United States Steel Corporation case (1920), the Alcoa case (1945), the United Shoe Machinery Corporation case (1953, 1968), and the IBM case (settled out of court in 1982).

In each of these instances, prosecutors attempted to prove that the accused firm was monopolizing or attempting to monopolize its industry. But in his book Antitrust and Monopoly, D. T. Armentano, a University of Hartford economist, shows that the defendants had gained their large market shares by offering lower prices and improved quality products to consumers.[6] Even for those firms eventually successful in defending their actions, Armentano notes, the costs in terms of legal fees and management time were substantial. Thus, the message sent to potential industry leaders was: "Compete, but not *too* successfully."

In their decisions, the antitrust courts often have confused the useful theoretical model of perfect competition with a realizable policy goal. As a result, they have distrusted corporate actions that placed smaller competitors at a disadvantage, regardless of how well consumers were served. The failure of even inefficient competitors would lead the industry further away from

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[5] Ibid., p. 211.

[6] Dominick T. Arementano, Antitrust and Monopoly: Anatomy of a Policy Failure (New York: John Wiley and Sons, 1982).

the stringent requirements of perfect competition. In short, the courts have sought to protect competitors rather than competition.

AN ALTERNATIVE MODEL: EFFECTIVE COMPETITION

Shortcomings of the Pure Competition Model

Assumptions in the "perfect competition" model about homogeneous products and complete information among buyers and sellers imply that firms compete only on the basis of price. But in reality, even practically identical products (toothpastes, for example) are perceived by consumers as having widely different characteristics. Furthermore, retailers' locations and the services they offer can be important means of differentiating products. And manufacturers often compete through the information or credit terms offered retailers and consumers, as well as through price.

In practice, actual markets are anything but the static creatures pictured by the pure competition model. Lacking complete information, business managers and consumers continually revise past decisions and attempt to correct earlier errors. Firms enter and leave the industry, new production and marketing processes are discovered, and consumer demand adjusts to new fashions, fads, economic conditions, and products.

Perhaps most important for the existence of competition in relatively concentrated industries, however, is that investors are constantly searching for a greater return on their funds. Thus, any industry that begins to earn an unusually high rate of profit will attract attention from individuals seeking to start new businesses and from existing firms wanting to expand their markets. Depending on the industry, new competitors may appear overseas as well.

This dynamic view of competition argues that cartels are extremely difficult to establish or maintain. In the first place, the many facets of the competitive process--price, research and development, service after the sale, to name a few--make successful anticompetitive cooperation all but impossible. No cartel can possibly shut out all potential competition. In addition, merely the threat of competition reinforces the difficulties of establishing a successful cartel or of firms colluding to exploit domination of the market. Any successful cartel will, by definition, earn higher profits than the norm for similar industries. Barring government intervention preventing additional entries, therefore, an incentive will exist for new firms to enter. Unless each new entrant can be successfully included in the cartel, something that is highly unlikely, competition soon returns to the industry.

Similarly, any product or organizational advantage that allows one firm to earn unusually high profits causes existing

and potential competitors to scrutinize that firm's behavior to determine its secret. If these successful methods can be copied, they will be, thus providing consumers with more of the type of service or product they have rewarded with their patronage and reducing the likelihood of market exploitation. Even in those cases where superior innovation, management techniques, or efficiencies cannot immediately be duplicated, they should be rewarded with higher profits. Such rewards stimulate competition by encouraging other firms to continue searching for similar advantages.

The Emergence of a New Model

Observations of the highly competitive nature of markets outside the "perfect competition" mold cause many economists to question the desirability of using perfect competition as a benchmark. As the study of competition has become more sophisticated, evidence has grown that competition is a strong and pervasive phenomenon and that its influence is felt even when there are but two or three firms in an industry. For example, Dr. Paul Pautler, an economist at the Federal Trade Commission, recently searched economic literature for the expected correlations between market power and profits. Significantly, no such connection could consistently be shown.[7] This absence of evidence that market concentration implies market control supports the growing realization that active competition exists in open markets--regardless of the degree of concentration.

Implications for Antitrust Policy

This appreciation of a powerful and dynamic competitive process has led writers as diverse as M.I.T. economist Lester Thurow and Appellate Court Justice Robert Bork to suggest that U.S. antitrust laws be revised substantially.

The Thurow Prescription

In his 1980 book The Zero-Sum Society, Thurow describes the "futility and obsolescence" of American antitrust laws.[8] He argues, for example, that the growth of international trade makes it impossible to determine whether an effective monopoly exists by examining a firm's domestic market share alone. International competition causes even large U.S. firms to behave competitively, so prosecuting a corporation merely because it is large is likely to do little to promote the consumers' interests. Breaking up an IBM into three or four smaller companies, for instance, would benefit no one, in Thurow's view--except, possibly, foreign computer manufacturers. As a result, Thurow sees reduced trade

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[7] Paul Pautler, "A Review of the Economic Basis for Broadbased Horizontal Merger Policy," The Antitrust Bulletin, Fall 1983, pp. 571-651.

[8] Lester C. Thurow, The Zero-Sum Society (New York: Penguin Books, 1980), pp. 145-150.

barriers as a more effective means of ensuring competitive markets than continued reliance on outdated antitrust laws.

Thurow also argues that rising real incomes make it increasingly difficult to define relevant markets. Most American consumer purchases can hardly be classified as "necessities," and a wide range of close substitutes exist for almost every purchase. So it is naive to assume that consumers will not react quickly if a manufacturer tries to exploit his domination of a narrowly defined market. The Federal Trade Commission's case against ready-to-eat breakfast cereal manufacturers, concluded in 1981 after nine years, Thurow believes, was such an example of the market's being defined much too narrowly. In addition to cold cereals, any number of products can satisfy a consumer's need for an early morning meal--hot cereals, pastries, or bacon and eggs. These products should have been considered as competing with ready-to-eat cereals, and the threat of market domination viewed accordingly.

In Thurow's view, the existence of large conglomerate firms also contributes to the obsolescence of most antitrust policy. Conglomerates, with their diversified resources, are often able to enter a market even when substantial capital expenditures are necessary. This threat places a powerful check on even single-firm industries, and discourages them from engaging in monopoly pricing.

The Bork View

While Justice Bork uses a slightly different analysis in his book, The Antitrust Paradox, published in 1978, his conclusions resemble those of Thurow. Bork maintains that the antitrust laws were misinterpreted when early decisions emphasized protecting competitors rather than protecting consumers. Unfortunately, the importance of precedence in deciding legal cases ensured the perpetuation of this mistake. Bork believes, therefore, that most of the current problems with antitrust enforcement could be resolved by directing the courts to focus on the welfare of consumers. Improved productive or distributive efficiency would then be viewed as enhancing consumer welfare rather than constituting an undesirable "barrier to entry" or a pernicious "competitive advantage"--as seems to be the case in some antitrust courts.[9]

Using this more realistic view of antitrust goals, Bork identifies three categories of behavior with which antitrust enforcement should be concerned:

1) agreements by direct competitors or potential rivals to fix prices or divide markets in those cases where the agreements are not necessary for the integration of legitimate economic activity;

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[9] Bork, op. cit.

2) horizontal mergers leaving fewer than three significant rivals in any market; and

3) deliberate predation, i.e., charging prices below the variable cost of production with the specific intent of eliminating competitors and achieving monopoly power, though Bork warns against confusing hard competition with predation.[10]

In the same vein, Thurow concludes that there are only two roles for antitrust policy: banning predatory pricing and banning implicit or explicit cartels that either set prices or divide markets.[11]

THE PROBLEM OF INNOVATION

While criticism of the antitrust laws in general is growing, Congress has been particularly concerned with the impact of antitrust enforcement on innovation. As part of a loosely defined "industrial policy" package, legislative proposals have focused primarily on impediments to joint R&D ventures, but antitrust policy has been even more far-reaching in its detrimental effects on American innovation.

By seeking to force U.S. industry into an unrealistic, perfect competition mold, antitrust enforcers may be removing the means by which research and development is conducted. It was economist Joseph Schumpeter who first noted in 1942 that firms in a perfectly competitive industry have neither the funds nor the incentive to carry out extensive research and development.[12] This phenomenon can be seen in agriculture, the U.S. industry most closely approaching the perfect competition ideal. Farmers have relied almost exclusively on federal and state funds for R&D, and most major innovations have been developed and promoted either by the U.S. Department of Agriculture or the state land grant colleges and county extension services.[13]

More specifically, there exists an inherent conflict between antitrust laws and laws protecting such intellectual property as copyrights and patents. Patents and copyrights are designed to encourage innovation by granting a limited monopoly. But these supposedly legal monopolies have been challenged using the anti-trust laws, creating uncertainty about the value of "protected" intellectual property and subjecting those who should be rewarded

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10 Ibid., pp. 405-407.

11 Thurow, op. cit., p. 150.

12 Joseph A. Schumpeter, Capitalism, Socialism, and Democracy (New York: Harper, 1942).

13 For a more complete discussion of policy in this area, see Bruce Gardner, "Agriculture's Revealing--and Painful--Lesson for Industrial Policy," Heritage Foundation Backgrounder No. 320, January 3, 1984.

for their creative activity to extensive legal expenses defending their claims.[14]

For the most part, these antitrust challenges have been private suits brought by disgruntled competitors against industry leaders. Since the 1950s the number of private antitrust cases has steadily increased; they amounted to at least 94 percent of the antitrust cases brought every year during the 1970s.[15] The reasons: the court interpretations favoring competitors over competition, the treble damages available to successful litigants, and the advantages to less innovative firms of delaying the introduction of new products and processes. IBM, Xerox, and Eastman-Kodak were all the targets of such private suits, and DuPont faced similar charges brought by the Federal Trade Commission.[16]

Many antitrust attorneys and judges continue to view patents as undesirable barriers to entry. Betty Bock, Director of Antitrust Research at The Conference Board, notes that in various antitrust cases attacking patent holders, it has been argued that innovative leaders should be required to grant production licenses to competitors harmed by a significant technological development, and that industry leaders should be required to "predisclose" to competitors new products or processes. It has also been argued, she says, that leading innovators should not be allowed to pass along cost savings to customers when price reductions would make it more difficult for competitors to match R&D investments.[17]

Suggestions for Reform

A number of proposals have been suggested to reconcile these concerns. Then Assistant Attorney General for Antitrust William Baxter proposed several specific legal changes in his June 29, 1983, testimony before the Senate Judiciary Committee. First, he suggested, the courts should not condemn any patent or copyright licensing arrangement as a *per se* violation of the antitrust laws.[18] Rather an effort should be made to identify and give

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14 The antitrust problem in this area is compounded by loopholes in the patent laws which allow foreign infringements to be sold in this country. See Milton Copulos, "Improving Patents to Spur Innovation," Heritage Foundation *Backgrounder* No. 318, December 23, 1983.

15 Betty Bock, *et al.*, *Antitrust in the Competitive World of the 1980s*, Research Bulletin No. 112, The Conference Board, 1982, pp. 18-19.

16 Betty Bock, *The Innovator as an Antitrust Target*, *op. cit.*

17 *Ibid.*

18 "*Per se violations*" of the antitrust laws refer to those actions historically deemed to be so potentially harmful with so little chance of exhibiting redeeming social value that no defense is allowed. If competitors are found guilty of price fixing, for example, they are punished. The court is not interested in hearing any possible justifications for the action.

weight to possible procompetitive effects. Second, Baxter explained that the "misuse doctrine," i.e., the standards defining the legally acceptable use of patents, has been used in some courts to undermine the rights of patent and copyright holders on the flimsy basis of what seems to be unfair, anticompetitive behavior. He recommended that the courts be prevented from using this doctrine to deny patent or copyright enforcement, except when the conduct in question is a clear violation of antitrust laws. Finally, Baxter recommended closing the patent law loophole that allows the importation of products made outside this country through the unauthorized use of a patented process.[19]

Among the other suggestions put forward for resolving the conflict between antitrust and patent laws is that punitive treble damages be discontinued in antitrust cases.[20] Others have advocated that treble damages be awarded only where a per se violation is involved or that judges be given the option of imposing treble damages only in cases found to have particularly virulent anticompetitive effects. Some state courts have already moved to reduce the number of private cases by allowing judges to require plaintiffs to reimburse successful defendants for costs involved in defending against nuisance suits. A similar practice in cases involving the use of federal antitrust laws to challenge patents could well serve to reduce the number and cost of such cases.

Pending Legislation

Receiving attention on Capitol Hill are proposals to clarify the conditions under which joint R&D ventures may take place. Successful research and innovation seem to require an increasingly large portion of corporate budgets. Furthermore, given the uncertainty that a marketable product will actually result, the risk attached to these substantial expenditures can seem overwhelming for a single firm. To encourage firms to undertake the R&D necessary for success in an international setting, Congress is examining means by which firms may legally share the costs and risks of research projects through joint ventures.

The bills that have been introduced to clarify the status of joint R&D ventures take a similar approach. For example, S. 568, introduced by Senator Paul Tsongas (D-MA), would provide joint R&D ventures with the option of receiving an affirmative certification from the Justice Department, i.e., specific Justice Department approval upon reviewing the specifics of a proposed project,

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[19] Statement of William F. Baxter, Assistant Attorney General, Antitrust Division, before the Senate Judiciary Committee, June 29, 1983.

[20] The law provides that, as a punitive measure, firms found to be guilty of certain antitrust violations will pay those harmed three times the financial damages suffered.

while S. 737 and H.R. 1952, introduced by Senator Charles Mathias (R-MD) and Representative Michael Synar (D-OK) respectively, would provide automatic certification upon notification that the venture meets certain specified standards. The standards for certification in the Tsongas bill are generally more flexible than those contained in the Mathias bill.

The conditions with which acceptable joint ventures must comply are also addressed in the proposed legislation. For example, the length of the program, its organization, the eligibility requirements for participants, and the procedures under which resulting patents would be licensed are outlined, though the bills vary somewhat in the specifics. All the bills provide some protections for covered ventures from private antitrust actions and federal criminal charges.

While many analysts welcome the discussion of these changes as a step in the right direction toward broader antitrust reform, there appear to be problems with these specific proposals. In his June 1983 testimony, former Reagan Assistant Attorney General William Baxter, for instance, has criticized much of the pending legislation as too narrowly focused and risking unnecessary regulatory burdens through the oversight provisions. Baxter noted that the Administration's approach rejects the certification route, arguing that all joint research ventures fully disclosed to the government should receive protection from private suits and criminal charges by federal enforcers. Further, there is a fear that the mandatory licensing provisions will impair rather than promote competition.[21] Similarly, Thomas B. Leary of the National Foreign Trade Council warns that, to be sure proposed changes are effective and do not provide disincentives to innovations, care must be taken to keep certification standards as flexible as possible.[22]

Work continues on the wording of the bills to be reported out of the Committees. Attempts are being made to incorporate some of the criticisms raised by the testimony on the earlier versions of the proposed legislation.

RECOMMENDATIONS

There are clearly a wide range of actions that may be taken to provide needed antitrust reform.[23] A general revision of the antitrust laws should:

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21 Baxter statement, op. cit.

22 Statement of Thomas B. Leary, the National Foreign Trade Council, on Bills to Provide Antitrust Exemption for Joint Research Ventures, June 29, 1983.

23 A number of authors have called for the complete repeal of all antitrust laws. See, for example, Armentano, Antitrust and Monopoly and Fred L. Smith, Jr., "Why Not Abolish Antitrust?" Regulation, January/February 1983, pp. 23-28, 33.

1) Modify Section 2 of the Sherman Act to ensure that competitive success is not considered a violation of the antitrust laws. Active competition cannot exist without hurting some competitors. Indeed, the very essence of competition is to benefit consumers by eliminating the less efficient producers. Firms rewarded by consumers for providing better quality, a lower price, or enhanced service certainly should not be punished by the Justice Department or the Federal Trade Commission.

2) Spell out and narrow the "unfair methods of competition" provision of Section 5 of the Federal Trade Commission Act. The vague nature of the current law unnecessarily increases the risk faced by businessmen as they are subjected to <u>ex post facto</u> determinations of what is a legitimate or illegitimate way of doing business. The only clearly "unfair methods of competition" are those that involve illegal practices like enforcing a patent fraudently obtained or threatening physical violence to deter competitors.

3) Modify Section 7 of the Clayton Act to ensure neither firm size nor concentration of the industry are presumed to be anticompetitive practices. Using Section 7, mergers have been denied on the basis of "concentration ratios" that often have little or nothing to do with monopoly power. This has made it unnecessarily difficult to consolidate declining industries or achieve economies of scale necessary to compete effectively on world markets. Attention should, therefore, be directed more toward government imposed barriers to entry rather than market determined firm size.

4) Abolish the automatic trebling of damages in antitrust violations and adopt a "rule of reason" in establishing assessable damages. With more than 90 percent of the antitrust cases being brought by private litigants, a changed attitude at the FTC or Justice has little effective impact on the chances that a particular firm will face a court battle. To help ensure that those cases brought by private litigants are brought for sound reasons and not merely to harass successful competitors, treble damages should not be guaranteed even where violations are discovered.[24]

5) Remove current disincentives to innovation and research by making it clear that no use of a patent or copyright lawful under the "intellectual property" laws should be

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24 For a more complete discussion of these first four and similar suggestions, see Richard B. McKenzie, editor, <u>A Blueprint for Jobs and Industrial Growth</u> (Washington, D.C.: The Heritage Foundation, 1984), pp. 15-23.

considered a cause for action under the antitrust laws. In addition, immunity should be provided from all private antitrust suits and from government antitrust damage suits in the case of all joint R&D ventures fully disclosed to the government.

CONCLUSION

Before accepting the argument that foreign competitors have unfair advantages because of government subsidies or a cheap labor supply, Congress should examine the impact of U.S. antitrust policies on firms attempting to compete in world markets. Strict enforcement of U.S. antitrust laws often has discouraged innovation, decreased efficiency, and thereby weakened the ability of U.S. firms to compete. This, in turn, has encouraged companies to seek an alternative strategy--protectionism.

Moreover, successful innovators or firms that prospered by offering consumers better quality products at lower prices often have found themselves the target of antitrust suits precisely because consumers have rewarded their efficiency by purchasing their products and increasing their market share. Threatened and actual divestitures on these grounds have discouraged growth, often at the expense of consumers.

It is time to reexamine antitrust policies--for the good of the American consumers and to create a climate that allows U.S. firms to become more effective competitors in international markets.

In short, before blaming American industry for its failure to compete effectively or fairly, the federal government should recognize its own contribution to the problem in basing antitrust policy on a theory of the marketplace that bears little resemblance to the reality of competition.

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